

must not be altered. Additional acquired chattel security should be entered on the file copy of the security agreement or chattel mortgage and must be described on subsequent security instruments.

(c) *Unapproved dispositions.* Unapproved dispositions of security will be handled in accordance with §§1962.18 and 1962.49 of this subpart.

[50 FR 45783, Nov. 1, 1985, as amended at 58 FR 46075, Sept. 1, 1993; 61 FR 35930, July 9, 1996]

§ 1962.17 Disposal of chattel security, use of proceeds and release of lien.

(a) *General.* (1) The borrower must account for all security. When the borrower sells security, the property and proceeds remain subject to the Agency's lien until the lien is released. All checks, drafts, or money orders which the borrower receives for the sale of collateral listed on Form FmHA 1962-1 (available in any Agency office) must be payable to both the borrower and the Agency unless all Agency loan installments for the period of the form have been paid including any past-due installments. If the borrower disposes of collateral or uses the proceeds in a way not listed on Form FmHA 1962-1, the borrower will have violated the loan agreement, and the Government will not release its security interest in the collateral. Releases of sales proceeds will be terminated when the borrower's accounts are accelerated.

(2) Section 1924.56 requires that there must always be a current Form FmHA 1962-1 in the file of a borrower with a loan secured by chattels. If a borrower asks the Agency to release proceeds from the sale of chattels and there is a current Form FmHA 1962-1 in the file, the request will be approved or disapproved in accordance with paragraph (b) of this section. If the borrower's request for release is denied, the borrower must be given attachment 1 of exhibit A of subpart S of part 1951 of this chapter, a written explanation of the reasons for the denial, and the opportunity for an appeal in accordance with 7 CFR part 780. Immediately upon determining that the borrower does not have a current Form FmHA 1962-1 in the file, the County Supervisor will im-

mediately contact the borrower to develop one.

(3) If the borrower requests a change(s) to Form FmHA 1962-1, and the County Supervisor can approve the change(s), the borrower and the County Supervisor will initial and date each change in accordance with item (6) in the Forms Manual Insert (FMI) for Form FmHA 1962-1. The form will be marked "Revised" and the borrower will be notified in writing confirming that the change(s) has been approved.

(b) *Use of Form FmHA 1962-1.* (1) County Supervisors are authorized to approve or disapprove dispositions of Agency chattel security in accordance with this subpart. The County Supervisor, with the assistance of the borrower, will complete Form FmHA 1962-1 in accordance with the FMI (available in any Agency office) to show how, when, and to whom the borrower will sell, exchange, or consume security and use sale proceeds (include milk sale proceeds). Government payments, crop insurance and insurance proceeds derived from the loss of security will also be accounted for on Form FmHA 1962-1. This includes, for example, sale proceeds on hand and crops in storage. Only the proceeds from the sale of normal income security can be used to pay essential family and farm operation expenses. Proceeds from the sale of basic security will not be used for essential family living and farm operating expenses. In addition to payment of prior liens, basic security can only be released for the purposes listed in paragraphs (b)(2)(iv) through (b)(2)(vii). When proceeds from the disposition of normal income security are to be used to pay essential family living or farm operating expenses, County Supervisors must approve the disposition. Any disposition of basic or normal income security must be recorded on Form FmHA 1962-1. However, the borrower is responsible for providing the County Supervisor with the necessary information to update the Farm and Home Plan and Form FmHA 1962-1.

(2) Under all circumstances, sales proceeds must be remitted to creditors with liens on the proceeds, in order of priority of those liens. Proceeds which are released by a prior lienholder or which are in excess of the amount due

to prior lienholder and which come to the Agency can be used as follows:

(i) The Form FmHA 1962-1 must provide for releases of normal income security so that the borrower can pay essential family living and farm operating expenses. However, proceeds from the sale of basic security will not be used to pay essential family living or farm operating expenses.

(ii) Essential expenses are those which are basic, crucial or indispensable. The following items are guidelines of what normally may be considered essential family living and farm operating expenses:

Household operating
Food, including lunches
Clothing and personal care
Health and medical expenses, including medical insurance
House repair and sanitation
School, church, recreation
Personal insurance
Transportation
Furniture
Hired labor
Machinery repair
Farm building and fence repair
Interest on loans and credit or purchase agreement
Rent on equipment, land, and buildings
Feed for animals
Seed
Fertilizer
Pesticides, herbicides, and spray materials
Farm supplies not included above
Livestock expenses, including medical supplies, artificial insemination, and veterinarian bills
Machinery hire
Fuel and oil
Personal property tax
Real estate taxes
Water charges
Property and crop insurance
Auto and truck expenses
Utilities payments
Payments on contracts or loans secured by farmland, necessary farm equipment, livestock, or other chattels
Essential farm machinery. An item of essential farm machinery which is beyond repair may be replaced when the County Supervisor determines that replacement is a better choice than alternatives such as the lease of a similar piece of machinery or the hiring of the service.

(iii) All of the items in paragraph (b)(2)(ii) of this section may not always be considered essential for every family and farming operation. County Supervisors must consider the individual

borrower's operation, what is typical for that type of operation in the area administered by the County Supervisor, and what would be an efficient method of production considering the borrower's resources. County Supervisors will refer to exhibit E of this subpart for guidance in determining whether an expense will be considered essential and the amount of proceeds which should be released. When the borrower and County Supervisor cannot agree that an expense is essential, the County Supervisor will notify the borrower, in writing, of why the requested release was denied, including why it is not basic, crucial or indispensable to the family and/or the farming operation and will give the borrower an opportunity to appeal in accordance with subpart B of part 1900 of this chapter and paragraphs (a)(2) and (b)(5) of this section.

(iv) Proceeds can be applied to the Agency debt.

(v) Proceeds can be used to purchase property better suited to the borrower's need if the Agency will acquire a lien on the new property. The new property, together with any proceeds applied to the Agency indebtedness, will have a value to the Agency at least equal to the value of the lien formerly held by the Agency on the old security.

(vi) Proceeds can be used to preserve the security because of a natural disaster or other severe catastrophe, when the need for funds cannot be met by other means or with an Agency loan or an Agency loan cannot be made in time to prevent the borrower and Agency from suffering a substantial loss.

(vii) Property can be exchanged, with prior Agency approval and in accordance with paragraph (b)(5) of this section, for property which is better suited to the borrower's needs if the Agency will acquire a lien on the new property, at least equal in value to the lien held on the property exchanged.

(viii) Property can be consumed by the borrower as follows:

(A) Livestock can be used by the borrower's family for subsistence.

(B) If crops serve as security and usually would be marketed, the County Supervisor can allow such crops to be

fed to livestock, provided, this is preferable to direct marketing and also provided that the Agency obtains a lien (or assignment) on the livestock and livestock products at least equal to the lien on the crops.

(3) The borrower must maintain records of dispositions of property and the actual use of proceeds and must make these records available to the Agency at the end of the period covered by the Form FmHA 1962-1, or when requested by the Agency. The County Supervisor will complete the "Actual" columns on that form, indicating approval or disapproval, making sure that the dispositions of property and uses of proceeds were as agreed upon. If they were not, the County Supervisor will take the actions required by § 1962.18 of this subpart. On the form, the County Supervisor will note approval or disapproval of each disposition.

(4) If, for any sale, the amount of proceeds actually received is above or below the amount of proceeds planned to be received as shown on Form FmHA 1962-1, the borrower will immediately notify the County Supervisor. If the borrower sells security to a purchaser not listed on the Form FmHA 1962-1, the borrower must immediately notify the County Supervisor of what property has been sold and of the name and business address of the purchaser. Such notification may be by telephone to the County Office, by letter, by visit to the County Office, or any other method the borrower chooses.

(5) If a borrower wants to dispose of chattel security which is not listed on Form FmHA 1962-1 or wants to dispose of chattel security in a way not listed in the "How" section or wants to use proceeds in a way not listed in the "Use of Proceeds" section on Form FmHA 1962-1, the borrower must obtain the Agency consent before the disposition or before the proceeds are used. The Agency *must* give consent for the release of normal income security if the change is necessary for the borrower to meet essential family living and farm operating expenses. The Agency *must* also give consent if the conditions set out on the form and in paragraph (b)(2) of this section are met. The borrower may obtain prior consent

by telephoning the county office, by letter, by visiting the county office, or by any other method the borrower chooses. When revisions are agreed to over the telephone, the County Supervisor *must* revise the Form FmHA 1962-1 contained in the borrower's case file, initial and date the change, and mark the form "Revised." The County Supervisor will then either write to the borrower and send a copy of the "Revised" form to the borrower asking the borrower to date and initial the change and return the form to the county office, or the County Supervisor will ask the borrower to date and initial the change the next time the borrower is in the county office. Changes that would result in a major change (examples of major changes are: Feeder pig to sow operation, cow/calf to feeder steer operation, dairy to row crop, etc.) in a borrower's operation will always require a visit to the county office so that the County Supervisor and the borrower can complete a new farm and home plan and revise Form FmHA 1962-1. The County Supervisor will be responsible for determining if the requested change is major or not. If a revision cannot be agreed upon, see § 1924.56 of subpart B of part 1924 of this chapter.

(c) *Release of liens.* (1) Liens will be released by the County Supervisor when security is sold, exchanged or consumed, provided the conditions set out on Form FmHA 1962-1 and in this subpart are met.

(2) Junior Agency liens on chattels and crops serving as security for Agency loans can be released when such property has no present or prospective security value or enforcement of the Agency lien would be ineffectual or uneconomical. The following information will be documented in the running case record:

(i) The present market value of the chattels or crops, as determined by the County Supervisor, on which the Agency has a valueless junior lien.

(ii) The names of the prior lienholders, amount secured by each prior lien, and the present market value of any property which serves as security for the amount. The value of all property which serves as security for amounts owed to prior lienholders must be considered to determine

whether the junior Agency lien has any present or prospective value.

(3) Liens obtained through a mutual mistake can be released. The reasons for the release must be documented in the running case record.

(4) Liens can be released when there is no evidence of an existing indebtedness secured by the lien in the records of the Agency, County, State, or Finance Office.

(5) Liens on separate items of chattels can be released to another creditor for any authorized Farm Credit Programs loan purpose when it has been determined by a current appraisal that the value of the remaining security is substantially greater than the remaining Agency debt.

(d) *Processing the release of chattel security.* (1) If the borrower or an interested third party requests a release of specific items which must be recorded under the UCC or chattel mortgage laws, Form FmHA 462-12, "Statements of Continuation, Partial Release, Assignments, etc.," Form FmHA 460-1, "Partial Release," or other Forms approved by OGC and required by State statute will be used. Care must be used to be sure that only specific items are released; for example, if a borrower requests a release of five cows, make sure that not all the cattle are released from the Agency lien. When specific items are listed on the security agreement, the County Supervisor should record the disposition on the *work copy* of the security agreement and on Form FmHA 1962-1.

(2) Assignments and consent to payment of proceeds will be processed under subpart A of part 1941 of this chapter and recorded on Form FmHA 1962-1.

(i) When it is necessary to temporarily amend Form FmHA 441-18, "Consent to Payment of Proceeds From Sale of Farm Products," or Form FmHA 441-25, "Assignment of Proceeds From the Sale of Dairy Products and Release of Security Interest," Form FmHA 462-9, "Temporary Amendment of Consent to Payment of Proceeds From Sale of Farm Products," will be used. All amendments of assignment agreements will be made on forms approved by OGC. The State Director will issue a State Supplement with the ad-

vice of OGC and prior approval of the National Office on the use of other forms. The original form after completion will be forwarded directly to the person or firm making the payment against which the assignment is effective, and a copy will be kept in the borrower's case file. All amendments of assignment agreements will be approved and recorded on Form FmHA 1962-1. Conditions of this section must be met. The County Supervisor will see that payments are made in accordance with the original consent when the amendment period expires. Normally, a temporary amendment will not exceed a six month period.

(ii) When the Agency is not expecting payment from the proceeds of a product on which it has a lien but the purchaser of the product inquires about payment, a letter should be written to the purchaser as follows:

The FmHA has a security interest in the (name of product) being sold to you by (name and address of borrower), but at the present time is not looking to the proceeds from the sale of that product for payment on the debt owned to this agency. Therefore, until further notice, it will not be necessary for you to make payment to the Agency for such product.

(e) *Releases of liens on wool and mohair marketed by consignment—(1) Conditions.* Liens on wool and mohair may be released when the security is marketed by consignment, provided all the following conditions are met:

(i) The producer assigns to the Agency the proceeds of any advances made, or to be made, on the wool or mohair by the broker, less shipping, handling, processing, and marketing costs.

(ii) The producer assigns to the Agency the proceeds of the sale of the wool or mohair, less any remaining costs in shipping, handling, processing, and marketing, and less the amount of any advance (including any interest which may have accrued on the advance) made by the broker against the wool or mohair.

(iii) The producer and broker agree that the net proceeds of any advances on, or sale of, the wool or mohair will be paid by checks made payable jointly to the producer and the Agency.

(2) *Authority.* The County Supervisor may execute releases of the Government's lien on wool and mohair on Form FmHA 462-4, "Assignment, Acceptance, and Release." Since Form FmHA 462-4 is not a binding agreement until executed by all parties in interest, including the producer, the broker and the Government, the County Supervisor may execute it before other parties sign it.

(f) *Notice of termination of security interest to purchasers of farm products* on consents or assignments upon payment in full. County Supervisors will notify purchasers of farm products as soon as the Agency has received payment in full of indebtedness for collection of which it has accepted assignments or consents to payment of proceeds from the sale of the farm products. When Form FmHA 441-18 is in effect under the UCC, the notice to the purchaser will be made on Form FmHA 460-8, "Notice of Termination of Security Interest in Farm Products." When assignments have been used, the notice to the purchaser will be by letter or by forms prescribed by State Supplements.

(g) *Release of Agency interest in insurance policies.* When an Agency lien on property covered by insurance has been released, the County Supervisor is authorized to notify the insurance company of the release.

[50 FR 45783, Nov. 1, 1985, as amended at 51 FR 13481, Apr. 21, 1986; 52 FR 32121, Aug. 26, 1987; 53 FR 35784, Sept. 14, 1988; 56 FR 15824, Apr. 18, 1991; 57 FR 18680, Apr. 30, 1992; 57 FR 60085, Dec. 18, 1992; 58 FR 46075, Sept. 1, 1993; 61 FR 35930, 35931, July 9, 1996]

§ 1962.18 Unapproved disposition of chattel security.

(a) *General.* When the County Supervisor learns that a borrower has made a disposition of chattel security in a manner not provided for on Form FmHA or its successor agency under Public Law 103-354 1962.1 or becomes aware of the misuse of proceeds by a borrower, corrective action must be taken to protect the Government's interest.

(b) *Notice to borrowers.* When a borrower has not properly accounted for the use of proceeds from the sale of chattel security, the County Super-

visor must request restitution by use of a letter similar to Guide Letter 1962-A-5.

(1) If the borrower makes restitution or provides sufficient information to enable the County Supervisor to post-approve the transaction on Form FmHA or its successor agency under Public Law 103-354 1962-1, no further action will be taken against the borrower. Post-approval can only be given under the conditions set out in 1962.17(b) of this subpart. Only one such transgression can be allowed in any period covered by the Form FmHA or its successor agency under Public Law 103-354 431-2, or other similar plan of operation acceptable to FmHA or its successor agency under Public Law 103-354, between annual security inspections, whichever is appropriate, and this must be made clear to the borrower.

(2) If the borrower does not make restitution, if the County Supervisor cannot post-approve the transaction, or if the borrower makes a second unauthorized disposition of security or a misuse of proceeds after settling the first offense as provided in paragraphs (a) and (b) of this section, the County Supervisor will proceed in accordance with § 1962.49 of this subpart.

[54 FR 14791, Apr. 13, 1989]

§ 1962.19 Claims against Commodity Credit Corporation (CCC).

This section is based on a Memorandum of Understanding between CCC and FmHA or its successor agency under Public Law 103-354 (see Exhibit A of this subpart). The memorandum sets forth the procedure to follow when producers sell or pledge to CCC as loan collateral under the Price Support Program, commodities on which FmHA or its successor agency under Public Law 103-354 holds a prior lien, and when the proceeds, or an agreed amount from them, are not remitted to FmHA or its successor agency under Public Law 103-354 to apply against the producer's indebtedness to FmHA or its successor agency under Public Law 103-354. In addition to the procedures outlined in Exhibit A, the following apply:

(a) *County Office action.* (1) Claims will not be filed with CCC until it is determined that the amount involved